

**TESTIMONY BEFORE
THE U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON TRANSPORTATION & INFRASTRUCTURE
SUBCOMMITTEE ON ECONOMIC DEVELOPMENT, PUBLIC BUILDINGS &
EMERGENCY MANAGEMENT**

BY:

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Madame Chairwoman and Members of the Subcommittee:

My name is John Hentschel. I am a member of the Counselors of Real Estate and President of Hentschel Real Estate Services, a real estate consulting and advisory firm that, among other things, advises government leaders in the U.S. and abroad about real estate valuation, and asset and portfolio management issues.

This testimony is based on the findings of a 2001 CRE Consulting Corps assignment commissioned by the Public Building Service (PBS) that was designed to independently assess PBS's portfolio management policies and procedures and compare its newly devised asset management strategy with the best practices employed in the private sector.

PBS's new strategy sought to shift its capital decision making process from a tactical to a strategic one. It envisioned that only self-sufficient properties that would be capable of producing revenues greater than operating expenses for the Federal Buildings Fund (FBF) would be retained and allotted funding for repairs, alterations and replacements (RAR). Those properties that failed to meet such criteria would be targeted for disposal.

The Counselors of Real Estate, an affiliate of the National Association of Realtors, is a professional society whose approximately 1,100 members are among the

world's most respected and highly qualified advisors on real estate matters. As a public service, the Counselors organized a *Consulting Corps* which provides strategic advice to Government Agencies and Non-Profit Organizations who seek strategies to resolve complex real estate problems.

The Consulting Corps employs a collaborative process for which CRE's volunteer their time and effort on a pro bono basis. For this assignment, I chaired a panel of CRE's that also included Mahlon Apgar, Howie Gelbtuch, Barbara Hampton, and Frank Livingston.

After reviewing relevant documents and briefing materials and conducting 5 days of intensive interviews and thoughtful deliberations the panel presented its findings and recommendations to the PBS Commissioner in a verbal report entitled "*An Agenda for Strategic Change*" on September 14, 2001, followed by the panel chairman's address to a conference of PBS Regional Administrators in Kansas City on November 6, 2001.

With respect to the PBS portfolio the CRE panel observed that:

1. In terms of **Age**, the Building Inventory was **old** with an average building age of more than 50 years and was below average in quality and physical condition.
2. In terms of **Productivity**, the income produced by the Building Inventory for the Federal Building Fund (FBF) was highly **stratified and concentrated** with 55% of the square footage generating 95% of the Funds from Operations.
3. The **Capital Needs** of the building inventory for RAR were **excessive** estimated by the GAO at the time to be in excess of \$4.0 Billion with many repairs having been deferred repeatedly and indefinitely.
4. **Availability of and Access to Investment Capital** to address the portfolio's RAR needs was extremely **limited**, well beyond the FBF's funding capacity, with

little prospect for direct Congressional appropriation, and few other identifiable sources.

5. Unlike the private sector, the **Legal and Budgetary Environment** within which PBS operated was highly structured, rigid, unsympathetic, and not amenable to change, modification, or exception.
6. In comparison to private sector standards, PBS's allocation of administrative **Overhead** to each building within the portfolio was **exorbitant** counteracting any benefits associated with self insurance and local property tax exemption.
7. PBS **lacked a strategic mindset**. Its narrow **caretaker focus** and preference for long term property ownership **conflicted with** PBS's stated **mission** and the federal government's **inherent budgetary and accounting bias** against capital investment reflected in its "scoring" rules, the absence of a capital budgeting process, and PBS's inability to retain disposition proceeds for other uses.

Unlike prior studies commissioned by PBS, the CRE Panel approached the issue from a much broader perspective that considered PBS's mission, funding, structure, systems and skill sets.

In addition to endorsing the adoption of PBS's more strategic approach to allocating its limited resources, the panel also recommended that PBS assume and demonstrate its capacity to perform a strategic leadership role as an advisor to help Congress, OMB and client agencies make informed real estate decisions. The panel further suggested that PBS should define and develop cost, efficiency and performance standards to guide real estate decisions.

Organizationally the panel believed that PBS should reduce redundancy and streamline regional entities, intensify management controls and institute uniformity and universal application of all processes, procedures and decisions.

Procedurally, the Panel felt that PBS should instill more discipline in its decision making process and introduce more rigor and uniformity in its analytical procedures. Among the panel's many suggestions were that PBS should compare and contrast the costs and benefits of leasing versus ownership (including the cost of RAR) on a net present value basis as well as calculating the Cost of Inertia (that is, Cost of Doing Nothing) for every property related decision. The panel also thought that adopting a 5 year capital budgeting process which compared and contrasted portfolio results with and without the expenditure of needed RAR investments, even if performed internally for informational purposes, would impose a level of fiscal discipline now lacking in the PBS analytical process. In the panel's view opportunities for outsourcing, especially the management of small, remote or isolated facilities, should be examined and encouraged whenever possible.

The Panel encouraged PBS to seek the authority to not only negotiate cancellation rights and purchase options in its lease agreements, but also the ability to segregate maintenance from new construction funds and retain property sale proceeds within the Federal Building Fund to fund RAR requirements.

In closing, the Panel commended PBS's foresight and its commitment to adopt contemporary asset management procedures. The Panel exhorted PBS to continually strive to achieve the efficient and balanced deployment of federal real estate assets by periodically evaluating portfolio contents and disposing of those that underperform established benchmarks to yield the most benefits at the least cost.

Thank you for your time and attention.

Respectfully,

John J. Hentschel CRE, MAI, FRICS

